

Exhibit 4

Addison Testimony

**BEFORE THE PUBLIC SERVICE COMMISSION OF SOUTH CAROLINA
COLUMBIA, SOUTH CAROLINA**

HEARING #16-11554 OCTOBER 12, 2016 10:30 A.M.

DOCKET NO. 2016-223-E:

SOUTH CAROLINA ELECTRIC & GAS COMPANY – Petition of South Carolina Electric & Gas Company for Updates and Revisions to Schedules Related to the Construction of a Nuclear Base Load Generation Facility at Jenkinsville, South Carolina

**TRANSCRIPT OF TESTIMONY
AND PROCEEDINGS**

VOLUME 3 OF 4

HEARING BEFORE: Swain E. WHITFIELD, CHAIRMAN; Comer H. ‘Randy’ RANDALL, VICE CHAIRMAN; and COMMISSIONERS John E. ‘Butch’ HOWARD, Elliott F. ELAM, Jr., Elizabeth B. ‘Lib’ FLEMING, Nikiya M. ‘Nikki’ HALL, and G. O’Neal HAMILTON

ADVISOR TO COMMISSION: F. David Butler, Esq.
Senior Counsel

STAFF: Joseph Melchers, General Counsel; James Spearman, Ph.D., Executive Assistant to Commissioners; Philip Riley, Doug Pratt, Lynn Ballentine, and Tom Ellison, Advisory Staff; Jo Elizabeth M. Wheat, CVR-CM/M-GNSC, Court Reporter; and William O. Richardson, Deborah Easterling, and Calvin Woods, Hearing Room Assistants

APPEARANCES :

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GISSENDANNER, ESQUIRE, MITCHELL WILLOUGHBY,
ESQUIRE, and BELTON T. ZEIGLER, ESQUIRE,
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1 **Q. PLEASE EXPLAIN WHY YOU BELIEVE THAT THE BLRA IS SO**
2 **IMPORTANT TO THE FINANCING PLAN FOR THE UNITS.**

3 A. The BLRA was adopted to make it possible for electric utilities like
4 SCE&G to consider building new nuclear units. Before the BLRA was
5 adopted, building a new nuclear plant was not a viable option for SCE&G.
6 For SCE&G to seriously consider adding new nuclear capacity, legislative
7 action was needed to overcome two major challenges. The BLRA sought to
8 address these two challenges, which are as follows:

9 **The Financing Challenge.** Recovering the financing costs of a
10 project during construction was the first challenge. During construction of a
11 base load plant, a company must raise hundreds of millions of dollars of new
12 capital each year to finance construction costs. Each time bonds are issued to
13 pay for construction, debt service increases. Unless there is a corresponding
14 increase in revenues, debt service coverage ratios decline as do other
15 financial ratios. Bond ratings are based on these ratios. As these ratios
16 decline, the creditworthiness of the company suffers. In time, bond ratings
17 are downgraded. At that point, raising capital on favorable terms can be
18 extremely difficult or potentially impossible. Capital to complete the plant
19 may not be available.

20 On the equity side, each time additional common stock is issued to
21 support construction, there are more shares outstanding. Additional
22 dividends must be paid. Without new revenues, earnings are diluted. As

1 earnings are diluted, the attractiveness of the stock and its value decline. To
2 finance the next round of construction, a higher number of lower-priced
3 shares must be issued to generate the same amount of capital. This causes yet
4 more dilution and further weakens the value of the stock going into the next
5 financing cycle.

6 The only solution is for the company to generate revenues sufficient
7 to pay debt service, meet coverage ratios and provide reasonable levels of
8 earnings per share as the new plant is built. Some years ago the Commission
9 recognized this fact and began to authorize utilities to include the financing
10 costs of plants in rates before they were completed. This was done in general
11 rate cases by recognizing the financing costs associated with construction
12 work in progress ("CWIP") as a revenue requirement for ratemaking
13 purposes. The Commission has historically allowed a company to apply its
14 weighted average cost of capital to its CWIP to determine the amount of
15 revenue needed to support the common stock and bonds issued to finance
16 construction. The weighted average cost of capital is the amount of revenue
17 that the Commission has determined to be necessary to support investment
18 of capital in the utility, specifically, to pay debt service on bonds and allow
19 a reasonable level of earnings to support common stock.

20 This CWIP based method of recovering financing costs required the
21 utility to file general rate cases stair stepped in one or two-year intervals
22 during plant construction. SCE&G successfully used this approach when

1 building its last coal plant, Cope Station (1995), and its most recent combined
2 cycle natural gas plant, Jasper Station (2004). During construction, there
3 were a total of six separate rate adjustments which placed some part of the
4 financial costs of the capital spent on those plants into rates.

5 Cope and Jasper, however, took three to five years to build, not
6 thirteen as is the case for nuclear. Outlays for those plants were in the
7 hundreds of millions of dollars, not billions. If this approach were to be used
8 to support a nuclear construction project, it would require SCE&G to litigate
9 full electric rate cases every year or two for approximately 12 years. Neither
10 SCE&G nor its investors considered this to be practical.

11 **Disallowances.** The second challenge utilities like SCE&G face in
12 base load construction is the threat of construction cost disallowances.
13 Investors are sensitive to very small changes in returns. Even ‘minor’
14 construction cost disallowances can hit investor returns with crippling force.
15 Furthermore, and maybe even more significant, is the fact that even a small
16 disallowance today indicates the potential for future disallowances as
17 construction progresses. Therefore, even small disallowances can drive
18 investors away and make it impossible for a utility to complete a construction
19 project due to lack of or inability to obtain financing at reasonable terms.

20 **The BLRA.** In response, the South Carolina General Assembly
21 adopted the BLRA. It allows for annual rate adjustments through revised
22 rates filings to cover the financing costs of approved nuclear construction

1 projects pending their completion. Financing costs are based on the same
2 weighted average cost of capital that applies under the CWIP method. As
3 with the CWIP method, before a plant goes into service, only financing costs
4 may be recovered under the BLRA, not the cost of the plant itself. The BLRA
5 carries forward the key concepts of the CWIP method but does so without
6 requiring full rate cases each year. Under ORS direction, the benefits of the
7 BLRA for customers were independently verified by a CPA firm in January
8 2016.

9 As to disallowances, the BLRA provides an opportunity for the
10 Commission to review the prudence of constructing the plant in detail before
11 construction begins. Once the prudence decision is made, disallowances are
12 permitted if (a) the construction does not proceed within the originally
13 approved cost and construction schedules and (b) schedule amendments such
14 as the updates that are requested here are not made. As to the second point,
15 the BLRA states that the Commission will grant requests for amendment as
16 long as “the evidence of record justifies a finding that the changes are not the
17 result of imprudence on the part of the utility.” S.C. Code Ann. § 58-33-
18 270(E)(1).

19 Under the BLRA, prudence reviews are made based on plans and
20 forecasts before construction begins. The Commission determines whether
21 or not it is prudent to proceed with the project under the construction plan
22 and with the contractors and the Engineering, Procurement, and Construction

1 (“EPC”) contract proposed by the Company. The initial plans and forecasts
2 can then be updated so long as the updates are not the result of imprudence
3 by the utility. This assures the financial community that disallowances based
4 on after-the-fact prudence challenges will not impair their ability to recover
5 the capital they invest in the project unless there is imprudence by the utility
6 in administering the project.

7 **Q. WHAT DO YOU BELIEVE TO BE THE POLICY BEHIND**
8 **LIMITING THE PRUDENCY REVIEW IN UPDATE DOCKETS TO**
9 **THE PRUDENCY OF THE OWNER IN MANAGING THE**
10 **PROJECT?**

11 A. In considering disallowances, the BLRA properly focuses on the
12 utility as owner of the project and those cases where the utility has caused
13 additional cost to be incurred through imprudence in its role as owner. More
14 specifically, in this project, the Commission properly looks to SCE&G as
15 owner for prudence in

- 16 • construction oversight;
- 17 • obtaining licenses and permits for the Units including Nuclear
18 Regulatory Commission licenses, and complying with those
19 licenses and permits;
- 20 • administering the EPC Contract and enforcing its terms;
- 21 • resolving disputes with the EPC contractors;
- 22 • constructing transmission facilities to support the Units;

- 1 • recruiting, hiring and training of operating staff for the Units;
- 2 • deploying information technology (“IT”) systems to support the
- 3 Units;
- 4 • drafting and obtaining approval of the operating, maintenance and
- 5 safety plans for the Units; and
- 6 • performing all the tasks that fall under the heading of operational
- 7 readiness for the Units.

8 The BLRA provisions as to cost and construction schedule updates
9 properly focus on those aspects of the project that the Company can control,
10 specifically its own prudence as owner in administering the EPC Contract,
11 overseeing the contractor’s work and performing the work that is the owner’s
12 direct responsibility. Other risks related to construction are reviewed in the
13 initial BLRA proceeding when the EPC contract, EPC contractor, and other
14 aspects of the project are being reviewed. The decision to approve a project
15 under the BLRA is a decision that it is reasonable and prudent to assume the
16 risks of proceeding given the terms of the EPC contract, the review of the
17 EPC contractor, and the other matters considered.

18 **Q. IS THIS POSITION CONSISTENT WITH THE COMMISSION’S**
19 **PRIOR RULINGS UNDER THE BLRA?**

20 **A.** Yes. In the 2008 proceedings, the Commission and the parties
21 reviewed the risk factors associated with this project and concluded that the

1 project should proceed under the terms of the BLRA in spite of those risks.

2 Based on its review of that information, the Commission ruled as follows:

3 The Commission's approval of the reasonableness and
4 prudence of the Company's decision to proceed with construction of
5 the Units rests on a thorough record and detailed investigation of the
6 information known to the Company and the parties at this time. Once
7 an order is issued, the Base Load Review Act provides that the
8 Company may adjust the approved construction schedule and
9 schedules of capital cost if circumstances require, so long as the
10 adjustments are not necessitated by the imprudence of the Company.
11 S.C. Code Ann. § 58-27-270(E). The statute does not allow the
12 Commission to shift risks back to the Company. ... In addition, risk
13 shifting could jeopardize investors' willingness to provide capital for
14 the project on reasonable terms which, in turn, could result in higher
15 costs to customers.

16
17 Order No. 2009-104(A), p. 92. On appeal, the South Carolina Supreme Court
18 described that order as "a very thorough and reasoned order." *Friends of*
19 *Earth v. Pub. Serv. Comm'n of S. Carolina*, 387 S.C. 360, 372, 692 S.E.2d
20 910, 916 (2010). The court stated that "the Commission addressed each and
21 every concern Appellant presented" *Id.*

22 **Q. WHAT INFORMATION ABOUT RISKS DID SCE&G PLACE**
23 **BEFORE THE COMMISSION IN 2008?**

24 A. When SCE&G filed for BLRA approval in 2008, it placed before the
25 Commission an extensive assessment of the risks and uncertainties of this
26 project. SCE&G also placed before the Commission its choice of EPC
27 contractors, its plan for construction of the Units, and the terms of the EPC
28 Contract under which subcontractors would be selected and the Units would
29 be constructed. SCE&G explained: